

# **CORPORATE RESOURCES OVERVIEW AND SCRUTINY COMMITTEE**

## ***Committee Report***

**Public**

**Date of Meeting:**

**6th December 2001**

**Title: COMMITTEE'S ROLE IN RELATION TO INTERNAL AND EXTERNAL AUDIT**

**Report of: The City Treasurer**

**Report reference: Fin. Memo 2001/02 No. 115**

**Summary: This report outlines the proposed programme and areas of work for Members of this Committee in relation to their overview and scrutiny role for Internal and External Audit.**

**Recommendations: Members are requested to :-**

- **Agree the proposed programme and areas of work for the Committee in relation to its role for the overview and scrutiny of Internal and External Audit as set out in this report and particularly in Appendix C.**
- **Note the role of Internal and External Audit as outlined in Appendices A and B.**
- **Note the Internal Audit Charter in Appendix D.**
- **Refer this report to the Management Committee for their information so that they are made aware of the detailed areas of scrutiny to be carried out by this Committee in relation to audit matters in accordance with the outline work – plan recently approved by the Management Committee.**

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Overview and Scrutiny Committee Financial Memo

Corporate Resources 2001/02 No. 115

6<sup>th</sup> December 2001

## **Members' Role in relation to Internal and External Audit**

### **1. Introduction**

1. In the Council's Constitution, the Corporate Resources Overview and Scrutiny Committee is responsible for the scrutiny of the financial workings of the Authority which encompasses Internal Audit matters.
2. The Constitution does not, however, spell out in detail the breadth of responsibility or the way in which it should be discharged by the Committee.
3. This report fleshes out the proposed detail of the role of the Committee in relation to audit matters in respect of both Internal and External Audit and provides the proposed protocols under which the Committee's role will be discharged.

1.4 Although not entitled "Audit Committee" in the singular sense, nonetheless the role of Audit Committee is clearly encompassed within the Committee's responsibility for scrutinising the financial workings of the Council. Section 2 of this report sets out the background to the role of Audit Committees.

### **2. Background to Recommended Practice for Audit Committees**

1. Following the publication of the Accounts and Audit Regulations 1996, the responsibility for providing the resources for the maintenance of an adequate and effective Internal Audit function moved from that of the Treasurer to that of the "relevant body". It remains, however, the responsibility of the Section 151 Officer (the City Treasurer in the case of Carlisle) to advise on the appropriate level of resources.
2. There is no statutory requirement for an Authority to have an independent Audit Committee. It is nevertheless the view of CIPFA, the Institute of Internal Auditors, the Audit Commission, the Best Value Inspectors and the Committee on the Financial Aspects of Corporate Governance (the Cadbury Committee) that such a Member forum should be set up in each Authority. The issue of the Committee's independence is in the context of not having responsibility for any services. Since the Committee's role is to hold the Executive to account in the use of corporate resources and to scrutinise the operation of the Authority's finances, this fits well with its proposed role as Audit Committee, undertaking the financial scrutiny functions normally associated with such a Committee.
3. The provision of Audit Committees in Local Government is gathering pace, in that the number of Authorities with such Committees has risen from 8% in the year 1996 to over 50% in 2000. It has been noted, from the recent Best Value Inspection reports relating to Internal Audit at Bridgnorth District Council and Flintshire County Council, that the Inspectors will expect to see a properly constituted Audit Committee, or a Committee which undertakes this role.
4. The Institute of Internal Auditors published a Position Statement in August 2000 stating that :-

*"current best practice recommends that organisations should establish a separate and independent Audit Committee".*

5. CIPFA's Code of Conduct for Internal Audit in Local Government defines the

Audit Committee as :-

*"a group of elected Members that fulfils the organisation's responsibilities and wishes in respect of the plans and findings of Internal and External Audit"*

6. The Code further states that :-

*"the Audit function should report, and be accountable to, the Audit Committee or equivalent"*

7. The Audit Commission's recommendations on Audit Committees, contained in their Bulletin "Protecting the Public Purse; Ensuring Probity in Local Government (1995 Update)", stated that :-

*"The Committee on the Financial Aspects of Corporate Governance (the Cadbury Committee) recommended that every listed company should establish an Audit Committee. The Audit Commission recognised the valuable role that such Committees could play in raising the profile of stewardship and probity within local government and recommended their establishment. Audit Committees should be established in all Local Authorities"*

### 3. The Roles of Internal and External Audit

1. The role of Internal Audit, as outlined in CIPFA's Code of Practice for Internal Audit in Local Government in the United Kingdom, is outlined in **Appendix A** to this report.
2. The role of External Audit is outlined as **Appendix B** to this report.

### 4. Programme and Proposed Areas of Work for the Committee

1. The programme and areas of work for the Committee which are proposed for Member's consideration are outlined in **Appendix C** to this report. If accepted, these should be recommended to the Council for approval.
2. In practice, many of the roles outlined in Appendix C will be undertaken by the Audit Manager in consultation with, or at the direction of, the City Treasurer as the Council's Officer charged with the proper administration of the Council's financial arrangements under S151 of the Local Government Act 1972. An update will be reported quarterly to the Committee.
3. Members are requested to note the "Internal Audit Charter" which is shown separately as **Appendix D** to this report.

### 5. Other Points for Consideration

1. The Audit Manager should attend meetings of the Committee at which Audit matters are to be discussed.
2. The Audit manager should be invited to any meetings between the City Treasurer and the Chair of the Committee when briefing or discussing any matters concerning the Committee's role on Internal Audit matters.

### 6. Timetable of Reporting to Committee

1. In terms of reporting, the following is the proposed annual timetable of events :-
  1. February – agree the Strategic (4- year) Audit Plan and the Annual Plan. Also agree the programme of Value for Money/Performance Review and Best Value studies, taking into account the views of the Executive where necessary.
  2. July – receive the first quarterly report on Internal Audit progress. Also receive details of disputed Grade "A" recommendations (i.e. those which relate to fundamental systems weakness/es) and details of any agreed recommendations which have not been implemented within the agreed timescale but for which no acceptable reason has been provided.

3. October – receive the second quarterly report as above.
4. January – receive the third quarterly report as above.
5. April – receive the final report for the preceding financial year.

## **7. Recommendation**

### **1. Members are requested to :-**

- 1. Agree the proposed programme and areas of work for the Committee in relation to its role for the overview and scrutiny of Internal and External Audit as set out in this report and particularly in Appendix C.**
- 2. Note the role of Internal and External Audit as outlined in Appendices A and B.**
- 3. Note the Internal Audit Charter in Appendix D.**
- 4. Refer this report to the Management Committee for their information so that they are made aware of the detailed areas of scrutiny to be carried out by this Committee in relation to audit matters in accordance with the outline work – plan recently approved by the Management Committee.**

D. Thomas

City Treasurer

November 2001

## **Appendix A**

### **The Role of Internal Audit**

#### **CIPFA Code of Practice**

CIPFA's Code of Practice (which is the standard against which the Authority will be judged by the External Auditor and the Best Value Inspectors in due course) states that :-

"Internal Audit is an independent appraisal function established by the management of an organisation for the review of the internal control system as a service to the organisation. It objectively examines, evaluates and reports on the adequacy of internal control as a contribution to the proper, economic, efficient and effective use of resources."

The Code also states that essential attributes for effective internal auditing are :-

#### **Independence**

The Internal Auditor should have the independence in terms of organisational status and personal objectivity which permits the proper performance of duties.

#### **Staffing and training**

The Internal Audit unit should be appropriately staffed in terms of numbers, grade, qualifications and experience, having regard to its responsibilities and objectives. The Internal Auditor should be properly trained to fulfil all responsibilities.

### Internal Audit Service Plan

The **key** objectives for Internal Audit are expressed in the Service Plan approved by the City Treasurer as :-

To determine whether adequate management controls are in place to ensure that assets are safeguarded, records are reliable, operations are efficient and policies and directives are adhered to.

To assist the City Treasurer in fulfilling his duties as the responsible officer under Section 151 of the Local Government Act 1972 which requires that every Local Authority shall appoint one of its officers to make arrangements for the proper administration of its financial affairs.

To ensure that the Authority's responsibility under the Accounts and Audit Regulations 1996, which require the maintenance of an adequate and effective Internal Audit function, is met.

Internal Audit also has the following **operational** objectives :-

To review the activities undertaken by the Council as a service to all levels of management; measuring, evaluating and reporting on the effectiveness of internal controls – financial and other – as a contribution to the efficient use of resources within the organisation, in order to :-

Safeguard assets

Ensure reliability and integrity of records

Promote operational efficiency

Monitor adherence to policies and directives

Accomplish objectives and goals

To continue to develop and promote the professionalism and quality of audit work and efficient and effective use of resources within the Audit Section.

To provide an efficient service that meets the needs of all clients.

To provide a place of work and conditions that ensure the health, safety and welfare of all employees whilst at work.

## The Role of External Audit

### Introduction

External Auditors for Local Authorities are appointed by the Audit Commission. For this Authority, this role is currently undertaken by District Audit.

District Audit's main objective as the appointed auditor is to carry out an audit which meets the Audit Commission's Code of Audit Practice. To ensure that their work is relevant to this Authority, one of the principal requirements of the Code is that they design a programme of work to address the significant operational and financial risks that are relevant to their audit responsibilities and which is agreed with the City Treasurer as the S.151 Officer.

The Code of Audit Practice, which has been produced for 2000/2001 following consultation with audited bodies, sets out three key objectives in relation to:

- the accounts
- performance
  
- financial aspects of corporate governance.

### The Accounts

District Audit are required to give a formal audit opinion on whether the Authority's accounts present fairly the financial position of the Authority and whether they have been prepared in accordance with statutory requirements.

They will do this by reviewing the Authority's core processes, namely:

- the main accounting system
- budgetary control procedures
- final accounts closedown procedures
  
- Internal Audit coverage of main financial systems.

They will also undertake detailed testing of material balances in the Statements of Account.

### Performance

District Audit are required to give a formal audit opinion on whether :-

- The Authority has complied with statutory requirements in respect of its Best Value Performance Plan
- The Authority has made adequate arrangements for securing economy, efficiency and effectiveness in the use of its resources
- The Authority has made adequate arrangements for collecting, recording and publishing specified performance information.

## Financial Aspects of Governance

District Audit are required to assess the adequacy of the Authority's arrangements for :-

- securing the legality of transactions that might have significant financial consequences
- ensuring that the Authority's financial standing is soundly based
- ensuring that the Authority's systems of internal control are adequate and effective
- ensuring proper standards of financial conduct are maintained
- preventing and detecting fraud and corruption

## Other Responsibilities

District Audit are also responsible for the certification of Grant Claims, and for answering questions from, and hearing objections from, members of the public.

## **Appendix C**

### **Corporate Resources Overview and Scrutiny Committee**

#### **Programme and Areas of Work in Relation to Audit**

#### **Internal Audit**

1. To consider and agree, on the advice of the City Treasurer, the scope and objectives of the Internal Audit Section, and to review and agree the Strategic (4 – year) and Annual Audit Plans. This will ensure that there is annual Member input to the Audit planning process and will also provide a forum for Members to request specific Audit reviews not included in the Plan.
2. To receive, consider and determine the priority of, requests for Value for Money, Performance Review and Best Value studies, having consulted with other relevant parties including the Executive.
3. To consider and recommend to the City Council that the resources made available to Internal Audit are sufficient to meet the Authority's needs, as recommended by the City Treasurer and/or the External Auditor.
4. To ensure that satisfactory arrangements are in place to promote economy, efficiency and effectiveness.
5. To review and recommend the Authority's policy relating to Theft, Fraud and Corruption, including being notified of any action taken under that policy.
6. To consider the objectives and scope of any additional work or investigations which Internal or External Audit are required to undertake, in order to ensure that Audit independence is not compromised.
7. To receive periodic reports from the Audit Manager in order to monitor progress against the Plan and key findings.
8. Where necessary, to discuss with the Executive, the City Treasurer and the Audit Manager the responses of departmental managers on major recommendations, in order to ensure that weaknesses in internal control are being addressed.
9. To determine the necessary action to be taken in those instances where, as a result of a follow - up review, it is noted that agreed recommendations have not been implemented and to require explanations from the relevant managers.

10. To provide a mechanism for informing Members of progress on high profile issues.

### **External Audit**

11. Along with the Executive, to review External Auditors' reports, consider matters arising and meet with the External Auditor as deemed necessary.

**CARLISLE CITY COUNCIL**  
**INTERNAL AUDIT SERVICES**  
**AUDIT SERVICES CHARTER**

## **CONTENTS**

1. Definition and Function
2. Authority and Independence
3. Role and Scope
4. Reporting Arrangements
5. Responsibility
6. Consultation
7. Documentation
8. Competence
9. Quality Control
10. Relationships with External Auditors
11. Amendment of Charter



**CARLISLE CITY COUNCIL**  
**INTERNAL AUDIT SERVICES**  
**AUDIT SERVICES CHARTER**

## **1 Definition and Function**

Internal Audit is a section of the City Treasurer's Department charged with providing an independent service both to Members and to all levels of management. The Audit Manager is responsible to the City Treasurer for the effective review of all aspects of risk management and control throughout the Authority's activities. Internal Audit also provides assurance to the Treasurer, as Section 151 Officer, as to the probity of financial transactions.

The primary function of Internal Audit is to review the activities undertaken by the Authority and to measure, evaluate and report upon the effectiveness of internal controls – financial and other – as a contribution to the efficient, effective and economic use of resources in order to :-

- Safeguard assets;
- Ensure reliability and integrity of records;
- Promote operational efficiency;
- Monitor adherence to policies and directives;
- Accomplish objectives and goals.

## **2 Authority and Independence**

The requirement for a Local Authority to set up and maintain an Internal Audit function is set out in Section 5 of the Accounts and Audit Regulations 1996. This states that "*a relevant body shall maintain an adequate and effective system of internal audit of their accounting records and control systems*". Internal Audit is independent of the activities which it reviews, in order both to ensure the unbiased judgement essential to its proper conduct and to enable it to offer impartial advice to management. Auditors should not undertake non-audit duties but where they do so, exceptionally, it is understood that they are not then functioning as auditors.

The Internal Audit function is established within the City Treasurer's department as part of the Financial services Division, answerable through the Head of Financial Services to the City Treasurer for providing an effective audit role. The Internal Audit function has no other responsibilities in supporting any of the services provided by the City Treasurer and thus its independence and objectivity are not compromised.

When required, the Audit Manager has direct access to the Town Clerk and Chief Executive and the Chair of the Corporate Resources Overview and Scrutiny Committee.

### 3 Role and Scope

The role of Internal Audit is to understand the key risks of the Authority and to examine and evaluate the adequacy and effectiveness of the system of risk management and internal control as operated by the Authority. The assessment of business risks is carried out jointly between management and Internal Audit and is reflected in the Strategic and Annual Plans which are endorsed by the City Treasurer, Senior Management and Members. Internal Audit has unrestricted access to all activities undertaken in the Authority - to people, systems, documents and property - in order to review, appraise and report on :-

- the adequacy and effectiveness of the systems of financial, operational and management control and their operation in practice in relation to the business risks to be addressed;
- the extent of compliance with, relevance of, and financial effect of, policies, standards, plans and procedures established by Members and management and the extent of compliance with external laws and regulations, including reporting requirements of regulatory bodies;
- the extent to which the Authority's assets and interests are acquired economically, used efficiently, accounted for and safeguarded from losses of all kinds arising from waste, extravagance, inefficient administration, poor value for money, fraud or other cause and that adequate business continuity plans exist;
- the suitability, accuracy, reliability and integrity of financial and other management information and the means used to identify, measure, classify and report such information;
- the integrity of processes and systems, including those under development, to ensure that controls offer adequate protection against error, fraud and loss of all kinds and that they align with the Authority's strategic goals;
- the suitability of the organisation of the units audited for carrying out their functions, and to ensure that services are provided in a way which is economical, efficient and effective;
- the follow-up action taken to remedy weaknesses identified by Internal Audit, ensuring that good practice is identified and communicated widely;
- the operation of the Authority's corporate governance arrangements.

Internal Audit should be consulted about significant proposed changes to internal control systems and the implementation of new systems.

Note: Internal Audit will assist managers in the following:

- ensuring, by the adoption of appropriate systems, the success of the Authority;

- ensuring the effectiveness of internal control;
- ensuring the reliability of financial reporting;
  
- ensuring, so far as reasonably practical, the absence of fraud or other irregularities, or that they are detected.

The above are, nevertheless, managers' responsibilities, and audit reviews do not relieve managers of the responsibilities assigned to them.

#### **4 Reporting Arrangements**

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A written report, in draft form, will be prepared and issued by Internal Audit at the conclusion of every review – this will be distributed to the Head of Service, the appropriate Director and the City Treasurer.

The report will normally include sections relating to :-

- introduction;
- objectives of the review;
- scope and method of review;
- audit points arising;
- conclusion;
- recommendations, suitably graded for their relative importance;
- a proposed timetable and officer responsible for the implementation of the recommendations.

The appropriate manager of the activity reviewed is required, under the terms of the Authority's Financial Procedure Rules, to respond to the draft report within 10 working days. This response should indicate the acceptance, or otherwise, of the findings and recommendations, and an action plan indicating clear accountability and timescales for implementing the agreed recommendations.

A final report will be issued indicating the manager's response, confirming the acceptance or rejection of the recommendations and incorporating the agreed action plan.

A follow – up review will be undertaken after approximately six months from the date of issue of the final report, in order to ascertain whether the agreed actions have been taken.

Any recommendations which have not been implemented, for which there is no acceptable reason for the delay, and any grade "A" recommendations which have not been agreed, will be reported to the Corporate Resources Overview and Scrutiny Committee for their

information and action.

Internal Audit reports regularly on the results of its work to the Corporate Resources Overview and Scrutiny Committee. The City Treasurer and the Audit Manager are accountable to the Corporate Resources Overview and Scrutiny Committee for :-

- providing regular assessments of the adequacy and effectiveness of the Authority's systems of risk management and internal control based on the work undertaken by Internal Audit ;
- reporting significant control issues and potential for improving risk management and control processes;
- periodically providing information on the status and results of the annual audit plan and the sufficiency of Internal Audit resources.

## **5 Responsibility**

The Audit Manager is responsible for :-

- developing strategic and annual audit plans based on an understanding of the significant risks to which the Authority is exposed. The audit plans will allocate resources to carrying out, as a minimum, an annual review of all of the Authority's major financial systems;
- submitting the strategic and annual audit plans to the Corporate Resources Overview and Scrutiny Committee for review and agreement;
- implementing the agreed audit plans;
- a review of the Authority's Best Value arrangements to ensure compliance with statutory guidelines;
- ensuring that the Audit Team operates to the "Code of Practice for Internal Audit in Local Government in the United Kingdom" which is published by CIPFA;
- maintaining a professional audit staff with sufficient knowledge, skills and experience to carry out the plan. (Refer to section 8 following relating to "Competence")

## **6 Consultation**

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Prior to the commencement of audit reviews, the Audit manager will arrange for the manager of the area under review to be advised as to the purpose, scope and expected duration of the work. A starting date will also be agreed.

During the progress of the review, internal Audit staff will consult – orally or in writing – with the relevant departmental officers to ensure that :-

- Information gathered is accurate and has been properly interpreted;
- Management are allowed to put their case in order to ensure the formation of a balanced judgement;
- Recommendations are cost effective and practicable;
- Management are informed on the progress of the audit.

## **7 Documentation**

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An adequate record of each audit review will be maintained, which will contain the principal evidence to support the Internal Audit report, and will provide the basis for a review of Internal Audit's work.

This record will, inter alia, contain adequate working papers to document the following :-

- audit planning;
- examination and evaluation of the adequacy and effectiveness of internal controls;
- audit procedures employed, information obtained, testing undertaken and conclusions reached;
- correspondence and/or formal post – audit interview/s;
- draft and final reports;
- evidence of the Audit Manager's review;
- agreed recommendations;
- follow – up review/s.

## **8 Competence**

The Audit Manager will maintain relationships with professional organisations and other bodies in order to keep abreast of current thinking and advances in Internal Audit practices.

The Audit Manager is responsible for maintaining a team of staff who collectively possess the necessary knowledge, skills and disciplines required for the achievement of the Internal Audit objectives.

In particular, the Audit Manager will, both by continuous appraisal and by means of a formal annual Personal Development Interview :-

- ensure that audit staff possess appropriate qualifications and experience;

- encourage staff and facilitate their continuing professional development.
- identify any further training required.
- as far as practicable, in order to maximise experience within the Audit Team, all Internal Audit staff will rotate the duties required from the Audit Plan, bearing in mind the size of the Team and the need for specialisation in specific areas.

## **9 Quality Control**

The Audit Manager will review the draft audit report and the associated working papers prior to the issuing of the report.

When the final report is issued, written feedback will be sought, by means of a Client Satisfaction Survey, from the recipient/s of the report. This feedback will be reviewed by the Audit Manager as a means of maintaining and/or improving audit practices and processes and as a means of identifying any necessary staff development.

Periodically – say every 3 or 4 years, a full consultation exercise will be undertaken with all of Internal Audit's "clients" to sure that the service given is meeting their expectations.

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## **10 Relationship with External Audit**

The Audit Manager will maintain liaison with the Authority's External Audit in order to :-

- foster a co – operative and professional working relationship;
- reduce the incidence of duplication of work;
- ensure that there is appropriate sharing of information;
- co – ordinate the overall audit effort;
- undertake compliance testing of core financial systems so as to provide the appropriate level of assurance to enable the External Auditor to place reliance on them for the purpose of issuing an unqualified audit certificate for the annual accounts.

In particular, the Audit Manager will :-

- discuss the Strategic and Annual Audit Plans with the External Auditor to facilitate audit planning;
- receive copies of all External Audit communications to management;

- gain a knowledge of the External Auditor's programme and methodology;
- ensure liaison, where appropriate, with External Audit for the purpose of resolution of differences.

## **11 Amendment of Audit Charter**

The Audit Manager is responsible to the City Treasurer for maintaining the Audit Charter in a current state.

Amendments to the Charter will be reported to the Corporate Resources Overview and Scrutiny Committee.

I. Beckett

Audit Manager

November 2001